Reviews - Writings in Accounting

Marie E. Dubke

REVIEWS

Writings in Accounting

DR. MARIE E. DUBKE, CPA, Editor
Memphis State University
Memphis, Tennessee

"*Decision Models,*" James C. Emery; DATAMATION; Vol. 16, No. 10, September 1, 1970

Although it is fairly well understood by now that routine processing systems yield fairly marginal returns, routine data processing applications are still the most common. However, Mr. Emery believes that current technology favors those applications that more fully exploit the capacity of the central processor. An example is using models to apply the computer directly to the decision making process. He states that the aim of the model builder is to describe the problem in a mathematical form that permits the calculation of the optimum decision out of all possible alternative decisions.

There are three requirements for using an optimizing model. The problem must be expressible in mathematical form. It must be possible to duplicate the real world in mathematical form with sufficient accuracy so that results from the model will make sense. This is complicated by uncertainty, large numbers of decision variables, and constraints.

The second requirement is that there must be explicit measure of the objective to be optimized. In many cases the objective is not obvious. Lower level managers are often faced with multiple objectives.

Third, there must be available a computational feasible procedure for finding the optimum solution. The mathematical equations that form the model must be manipulated in order to determine the values of the decision variables that optimize the objective function.

Mr. Emery concludes that models can be helpful in MIS optimization decisions and that the feasibility of a given optimizing procedure depends on the state of the art in both computer technology and computational methods.

Dr. Patricia L. Duckworth, CPA
Metropolitan State College

Editor's Note:

The Emery article should be interesting to all who enjoyed "Corporate Models: The Next Step?" beginning on page 5 of this issue.

"*Divisional Performance: Measurement and Control,*" David Solomons; Richard D. Irwin, Inc., Homewood, Illinois; 1970, 307 pages.

The book reports on a study sponsored by Financial Executives Research Foundation investigating the financial relations existing between the central management of a divisionalized company and the management of its several divisions. As a result of such investigation, the author arrives at recommendations which he feels would make for the more effective coordination and control of divisional operations.

The book reviews the organization of divisionalized business; the division of authority and responsibility between staff departments and divisions was also given special emphasis. There are many organizational choices available—from complete divisional autonomy at one extreme to complete and detailed domination of divisional management by the president and his staff at the other extreme. Professor Solomons points out that the degree of delegation which suits one company may not suit another.

The author agrees that pinpointing responsibility for a cost in measuring divisional performance is often difficult. Responsibility accounting in divisional companies is very much concerned with the allocation of costs and revenues to the functions and persons responsible for them in the business. This accounting activity is concerned with the evaluation of past performance as well as with the motivation of managers to conduct their operations in a manner to serve the company's best interests. He emphasizes that, where responsibility for the incurrence of a cost is shared by two departments, it should be charged to the department which will accept the invoice or pay the labor.

The author concentrated on the aspects of financial control which are peculiar to the divisional form of organization. Last-in first-out basis of inventory valuation, direct costing, and accelerated methods of depreciation accounting were discussed in relation to divisional profit measurement. Illustrations were used to show the advantages of using direct costing to measure a division's performance.

The book contains excellent information concerning interdivisional relationships which is one of the features of decentralization. Since divisions deal with each other, a decision must be reached concerning the transfer price to use. The use of accurate transfer prices is essential to help management evaluate the performance of the profit centers when they are viewed as separate entities. However, transfer prices must also motivate the division to act in a manner which is conducive to the success of the company as a whole. The author emphasizes that managers must be aware of the dangers of suboptimization because there often is a real conflict of interest between maximizing a division's profit and maximizing the overall company's profit. Graphs are effectively used to show the advantage of using one transfer price basis as opposed to another.

Professor Solomons pointed out that divisionalization is not always the right organization as there is a danger of duplication of authority. There are other dangers; it is not suitable for companies of all sizes in all situations. *Certainly a business firm that is contemplating decentralization should review this book to learn of all the aspects of this organizational pattern.*

Dr. L. Gayle Rayburn, CPA
Memphis State University

"Leaders Across the Ocean: Comparing American and European Chief Executives," **H. C. de Bettignies, EUROPEAN BUSINESS, Summer, 1970.**

Mr. Bettignies asks the questions, "Who are the leaders of big corporations on both sides of the Atlantic? Do different environments have an effect on the men at the top in American and European firms? Can this difference explain, even partly, the economic achievements of one country as opposed to those of another? What lessons can be learned from the experience of others?"

In an attempt to answer these questions, the personal and professional characteristics of top managers in the largest corporations in France, Great Britain, Germany, Italy, Belgium, and the Netherlands were investigated and compared with characteristics of American executives.

It is pointed out that it is difficult to produce a profile of the European top executive because there are many significant differences in the education, social origins, and career patterns of top executives in different countries. Mr. Bettignies quotes the May 1970 issue of *Fortune* which said that the highest executives of very large United States corporations remain something of an enigma. Information was obtained about 492 of the presidents of the largest U.S. corporations in 1966 from Heidrick and Struggles, an international management consulting firm. The European data was obtained by means of a survey which brought 576 answers from the chief executives of the 500 largest international companies in England, France, Germany, and Italy, and of the 250 largest in Belgium and the Netherlands.

The survey showed that the American president is younger than his European counterpart. Only 25% of the American company presidents are over 60, but 40% of the European presidents are past 60. French and Belgian executives are the oldest.

The survey showed that social barriers are falling in America, but not in Europe. In 60 years the proportion of American chief executives from the middle and lower classes has soared from over 50% to 90%. In European companies today, only 5% of the chief executives are from the lower class while 16% are from the middle class. Among the leaders of the 500 largest U.S. corporations in 1964, 5.8% succeeded their fathers in the top position; in the largest European firms 26.4% followed fathers, while in France the figure was 34.2%.

Americans and Europeans alike have scientific training. American executives are increasingly graduates of business schools; European presidents, although largely majoring in engineering or scientific fields, still study the humanities.

American executives tend to be more mobile than their European counterparts, but mobility on either side of the Atlantic does not seem to be strikingly high. The least mobile men are the British (46% have risen within the same company), followed by the Dutch. The most mobile by far are the Germans, 41% of whom have changed companies more than three times. One out of four Italian presidents has worked in three or more companies.

Europeans reach the top sooner than the American presidents. The average age at appointment to the top position is 47 in Europe and 50 in the United States. European presidents tend to remain in the top position longer than those in the United States. The American president will retire earlier or leave for another top job.

In regard to salaries, the American's pay starts where the European's ends. The American chief executive's lowest pay starts at $50,000 with the mean between $100,000 and $150,000 and the highest at $200,000. Presidential salaries in Europe range from less than $25,000 to more than $48,000. In Germany 47% of the top executives earned more than $48,000, but only 10% in Italy exceeded the $48,000 figure.

Mr. Bettignies believes that in comparing European and American top executives we see more common features than differences. He also thinks that the Europeans tend to invent more differences than really exist between American top managers and themselves and that only a study of top executives' attitudes in Europe and America will cause significant differences to emerge. *It appears to this reviewer, however, that America is still the land of opportunity for the person who wishes to get to the top.*

Mary E. Burnet, CPA
Rochester Institute of Technology

***"The Accounting Review, Supplement to Volume XLVI 1971,"* American Accounting Association, Evanston, Illinois.**

Many accountants know less about the American Accounting Association than the American Institute of CPAs. Operating on a much smaller budget and with many fewer employees, AAA has, nonetheless, sponsored and produced outstanding publications on accounting theory which have become "classics" in the accounting world.

Recently a voluminous paperback (350 pages) was mailed to all regular members of the Association. It contains reports from seven 1970-71 committees of the Association. The committees are:

1. Foundations of Accounting Measurements
2. Accounting Theory Construction and Verification
3. Accounting for Not-for-Profit Organizations
4. Non-Financial Measures of Effectiveness
5. Measurement Methods Content of the Accounting Curriculum
6. Behavioral Science Content of the Accounting Curriculum
7. Accounting and Information Systems.

Two practitioners and one governmental employee sat on the Not-for-Profit Organizations and the Information Systems Committees. All other members on all committees were from universities.

Some of the topics and areas investigated are being considered by the APB. Two of the committees' reports will be of special interest to those in the teaching field. Yet the accounting curriculum is too important to be left only to educators; those in practice should be interested, concerned and vocal. Professor S. I. Hayakawa (President, San Francisco State College) has emphasized in his syndicated column and in speeches that educational institutions become better when those with experience in the real world participate both as students and teachers!

Some of the recommendations made by various committees may appear impractical, academic and inapplicable. Other parts of the reports seem more related to other disciplines than to accounting.

The reports of these committees are recommended to our readers, not because the recommendations will become required in annual reports after a certain time as is true of APB opinions; rather this reading is recommended to expose the reader to new ideas and different approaches and to promote communications between practitioners and outstanding accounting academicians. If their ideas are good, eventual changes in practice should result. If the ivory tower domain of the authors has made their vision myoptic, this information should be conveyed to them. Hopefully their ideas will spark new ideas or alternatives in practitioners.

The reports appear to be well prepared, the result of careful study and scholarly research. Several committees include weighty bibliographies which will be valuable to those who wish to study the areas in greater depth.

M.E.D.

***"Organizing, Operating, and Terminating Subchapter S Corporations,"* D. Larry Crumbley and P. Michael Davis; Estate Tax Publishing Company, Aberdeen, South Dakota; 1970, 306 pages, $16.00 (cloth cover.)**

This book explains in clear language how Subchapter S election allows a closely-held corporation to decrease its tax burden. The reader is also informed of the best methods of terminating an election if the circumstances indicate that the normal corporate form of taxation is advantageous. Visual aids and examples drawn from actual practice are incorporated throughout the book. This manual is intended to clarify the tax traps and dangers of Subchapter S election so it can be utilized by many of the myriad corporations that are closely held.

Since the Subchapter S election was added to the law in 1958, the number of electing corporations has increased substantially each year. In the first year of existence, many of the total returns were filed by loss corporations. The corporations made the election in order to pass losses to the stockholders' individual tax returns. Gradually more taxpayers became aware of this tax planning tool until a majority of Subchapter S returns are from profitable businesses. However, the authors feel that there are many potential corporations who, because of lack of knowledge of the owners, have not taken advantage of such an election. The purpose of this book is to alleviate this lack of general tax knowledge so that the earnings of a closely held corporation get to the stockholders with a minimum loss of profits through taxes.

This book discusses the legislative history and background of Subchapter S. The authors feel that the modern Subchapter S concept probably evolved from the numerous proposals to eliminate the harsh effects of double taxation of corporate income. When this opinion was combined with the idea that a closely held corporation is in reality a partnership, constructive action was taken.

The authors emphasize that not just any business organization can become a tax option corporation because the organization must meet stringent requirements involving stockholders and prohibitive income. These requirements must be continuously satisfied after the election is made, or the election will be terminated automatically as of the beginning of the tax year in which any requirement is no longer fulfilled. The book gives a unique annual checklist in order to help avoid the harsh consequences of an unintentional termination of an election.

Dr. Crumbley and Dr. Davis point out that a Subchapter S election is by no means permanent in the sense that it is binding upon the firm for the balance of its corporate life. The Subchapter S status may no longer be desired and the logical course of action would be to terminate the election and allow the corporate tax to be imposed. On the other hand, the corporation or its shareholders may create a situation whereby the corporation is no longer eligible for Subchapter S status. Since the shareholders are still taxed on the dividends that they actually receive, an involuntary termination of the Subchapter S election could become quite costly. Extensive tax planning prevents the termination. Much of the book discusses in a practical manner this tax planning.

The authors also include a checklist of advantages and disadvantages; they are quick to point out that the Subchapter S election is not a step to be undertaken haphazardly. The taxpayer who contemplates the election must realize that the return to the corporate form of taxation may well be impossible without substantial tax cost. The authors stress, however, that the election is too useful a tool to discard because of the complications that may arise, for the dangers may be reduced by a proper understanding of the numerous pitfalls. They believe that there is no general formula or rule that can be used to decide when a Subchapter S election should be utilized. Each business must be given individual attention.

Dr. L. Gayle Rayburn, CPA
Memphis State University

***"Better Prose: A Method,"* Herman R. Struck; Houghton Mifflin Co., Boston; 1965, 100+ pages, $2.75 (paperback).**

Chapters Three and Four of the paperback have been most helpful not only to this reviewer, but to numerous graduate students. (Your reviewer took a non-credit course at Michigan State University from Herman Struck, author of this paperback.)

Mr. Struck's techniques result in shorter, more active sentences—interesting papers instead of heavy reading. Instead of "A great part of a child's early years is spent in the school-learning situation," he recommends "A child spends most of his early years in school." Instead of "The result for the slow learner is usually discouragement and even the possibility of damage to his personality," he suggests "The result usually discourages the slow learner and may even damage his personality."

The booklet contains a number of exercises and their solutions. Charts are provided to make the writer his own critic.

Most accountants do not write easily. Most accountants need to write better. This paperback is a "do-it-yourself" guide to better writing.

If used as a study guide for an ASWA workshop, it might even increase the flow of better written articles to the Editor of THE WOMAN CPA!

M. E. D.